

VZCZCXYZ0000
OO RUEHWEB

DE RUEHTA #3318/01 3480927
ZNY CCCCC ZZH
O 140927Z DEC 07 ZDK CITING RUEHCB #6313 3481213
FM AMEMBASSY ASTANA
TO RUEHC/SECSTATE WASHDC IMMEDIATE 1367
INFO RUCNCIS/CIS COLLECTIVE PRIORITY 0337
RUEHRO/AMEMBASSY ROME PRIORITY 0373

C O N F I D E N T I A L ASTANA 003318

SIPDIS

SIPDIS

E.O. 12958: DECL: 12/14/2017
TAGS: [EINV](#) [ENRG](#) [EPET](#) [PREL](#) [KZ](#)
SUBJECT: CONOCOPHILIPS CEO SEES PROSPECTS FOR JOINT
OPERATORSHIP AT KASHAGAN

REF: (A) ASTANA 3281 (B) ASTANA 3226

Classified By: Ambassador John Ordway, Reasons 1.4 (b) and (d)

Summary

¶1. (C) ConocoPhillips CEO James Mulva told the Ambassador on December 13 that he sees prospects for a deal under which Eni will be replaced as Kashagan operator, with three of the larger consortium members developing the field as joint operators. All companies in the Kashagan consortium except ExxonMobil have agreed to increase the stake of KazMunayGaz (KMG) in the project. A negotiating group is working in London to establish the compensation due Kazakhstan for Kashagan delays and cost overruns. While in Kazakhstan, Mulva will also discuss with the GOK the results of a ConocoPhillips study of the country's gas transportation options and make a renewed pitch for a ConocoPhillips role at N-Block and the Northern Caspian Jurassic Block. End Summary.

Kashagan

¶2. (C) In a meeting with the Ambassador on December 13, ConocoPhillips CEO James Mulva discussed two key outstanding issues in the Kashagan dispute: operatorship and compensation for Kazakhstan. Mulva told the Ambassador that he sees the emergence of a deal under which three of the larger companies in the Agip Kashagan Consortium (which consists of Eni, Total, ExxonMobil, Shell, ConocoPhillips, and KazMunayGaz) will develop the field under a joint operator model, with perhaps one company taking the lead on each of the three main aspects of the project: on-shore, off-shore, and pipeline. A joint operatorship might require the creation of a new entity, which could be lightly staffed with just a dozen or so key people, he explained. According to Mulva, Eni may remain responsible for developing Kashagan's initial phase - and may even be left in place for the longer run as the formal operator, in order for the company to "save face." Full-field development, however, is beyond Eni's capabilities and must be performed by larger companies, contended Mulva. Since ConocoPhillips owns a smaller share than the others, it has decided not to take a leading role in the negotiations, and will accept what ExxonMobil, Shell, and Total work out.

¶3. (C) Mulva explained that the Kazakhstanis continue to ask for \$7 billion dollars in compensation for the Kashagan development delays. At a \$55 per barrel price for oil, the project is not even worth \$7 billion dollars, he argued. Thus, the consortium members have said no to this demand. Mulva said that all the companies except ExxonMobil have agreed to a dilution of their ownership share and thus an

increase in KMG's equity stake of 8.33 percent. The sides are negotiating in London to establish the value of the additional ownership stake. The companies expect that KMG would pay something for the stake, and the difference between the valuation of the stake and KMG's payment would be part of Kazakhstan's compensation. Mulva reminded the Ambassador that valuation is a very complicated process, requiring the sides to agree on a number of factors, including future oil prices and an appropriate discount rate.

¶4. (C) Mulva contended that the main issue for ExxonMobil is, in fact, what the fair market price is for KMG's increased share - hinting that in the end, ExxonMobil would agree to go along with dilution once this is worked out. (Note: During a December 3 meeting in Washington, ExxonMobil International Governmental Affairs Manager David Bailey told the Ambassador that ExxonMobil is prepared to agree to dilution if compensated. End Note.) Mulva explained that if ExxonMobil is offered a piece of the operatorship and the valuation issue is resolved, then the other companies will have more leverage to pressure ExxonMobil to finalize a deal. Mulva argued that all of the consortium members agree that "we need to get this done," particularly because further delays may force the consortium to shut down portions of the project. Even brief delays now may delay the project by several years, as equipment, supplies, and personnel are reallocated to other projects around the world.

ConocoPhilips Pushes for Additional Projects in Kazakhstan

¶5. (C) Mulva told the Ambassador that the main reason for his trip to Kazakhstan is, in fact, to lobby for a role for ConocoPhillips in two major off-shore projects and to discuss

the results of a ConocoPhillips study on gas. ConocoPhillips remains very interested in developing N-Block, said Mulva. Nevertheless, Kazakhstan still insists that it will undertake at least the initial project development on its own. ConocoPhillips has also conveyed its interest on the Northern Caspian Jurassic field and will continue to push for involvement, although Kazakhstan has received 15-20 other proposals, according to Mulva. In general, he said, Kazakhstan is delivering the message that it wants to solve Kashagan before discussing new projects.

¶6. (C) Mulva will also discuss with the Kazakhstanis the results of a study on Kazakhstan's gas performed by ConocoPhillips upon the suggestion of Prime Minister Masimov in June. Masimov expressed Kazakhstan's interest for further information on options beyond traditional exploration and development projects, including LNG, CNG, and pipelines. Nick Olds, Conoco Phillips Country Manager for Kazakhstan, reported that the study revealed that Kazakhstan's three best gas options are continued northern transport through Russia, a trans-Caspian option, and a pipeline to China. All other options, including LNG and CNG, make little economic sense.

Comment

¶7. (C) Mulva's comments, and President Nazarbayev's recent assurances to the Ambassador that Kazakhstan will not invoke its sub-soil law, strengthen our belief that the Kashagan dispute will be resolved through negotiations, although not likely before the latest December 20 deadline. Thus far, Kazakhstan has handled the negotiations skillfully, driving a hard bargain without scaring off investors, as witnessed by Mulva's visit to push for further investment in the country.

ORDWAY